BRI CONNECT: AN INITIATIVE IN NUMBERS

3RD EDITION

Understanding risks and rewards of infrastructure projects

refinitiv.com
SUMMARY

• The Belt and Road Initiative (BRI), launched by China, is playing a pivotal role in meeting the growing demand for infrastructure development globally.

• Refinitiv is tracking $3.16 trillion worth of active BRI projects that will require billions of dollars of financing. These projects, in turn, will require steel, cement raw materials, and ancillary services that would require funding as well.

• According to Refinitiv's BRI Database, transportation accounts for 47 percent of all BRI, while Russia is the top destination for BRI developments, in number and value terms, with 122 projects valued at $287 billion.

• BRI projects are no longer the preserve of Chinese state-owned companies (SOEs). Chinese private companies and publicly listed companies accounted for 20.5 percent and nearly 7 percent, respectively, of all funding for BRI projects. SOEs continue to play an important role, though, accounting for 46 percent of all funding.

• China is throwing open BRI to participation by international corporations, financial institutions, and professional firms as it rolls out an inclusive BRI 2.0.

• While debt sustainability of BRI projects remains a lingering concern, China last year published a BRI Debt Sustainability Framework (BRI DSF), which aims to enhance the analysis of debt sustainability, fiscal risks, and debt reporting transparency for BRI projects.

• On the other hand, participating governments also need to be mindful of their existing and projected levels of public debt and assess whether the additional public debt, measured against the broader economic benefits, is worth the extra risk.

• Chinese SOEs are placing a greater emphasis on commercial feasibility at an early stage and raising funds through more diverse sources such as international commercial banks, multilateral development banks, and other private sources of capital, in their search for more competitive sources of funding outside Chinese banks.

• China’s plans to transform itself into one of the leading forces of green finance and energy will benefit BRI countries as they transition to low carbon economies. China is the world’s largest producer, exporter, and installer of solar panels, wind turbines, batteries, and electric vehicles, placing it at the forefront of the global energy transition.

• Among the indirect benefits of Belt and Road is that countries on the route are becoming the go-to destinations for Chinese investors in non-infrastructure areas, ranging from real estate to manufacturing to fintech. For example, the UAE, the second-biggest economy in the Middle East, is now the eighth most popular country in the world for Chinese real estate buyers.
China’s efforts to tie the world together through ports, bridges, rail and infrastructure projects under its Belt and Road Initiative (BRI) continues to gain momentum.

The world’s second biggest economy closed 2019 strongly with $360 billion worth of Belt and Road projects announced in the fourth quarter, nearly double the third quarter’s figure of $185 billion. However, the number of projects announced dipped 17.7 percent Quarter-over-Quarter to 168, according to latest data from Refinitiv BRI Database, a part of Refinitiv’s Global Infrastructure Initiative.

All told, Refinitiv is now tracking $3.16 trillion worth of active BRI projects that will require billions of dollars worth of financing, apart from steel, cement raw materials and support from ancillary services. The boom is expected to benefit China’s infrastructure companies but also local economies that will be home to the major projects.

“In this world of interdependence, we must expand our thinking beyond all forms of nationalism to assume our common destiny. For all this, China will remain useful to the world,” Chinese President Xi Jinping told state-owned news agency Xinhua last year.
As many as $613.6 billion worth of projects have already been completed, while $20 billion worth of projects have been delayed. Just under 2 percent of the projects have either been put on hold ($64 billion) or cancelled ($12.56 billion), suggesting a high success rate of project conversion. Under Refinitiv’s BRI methodology, delayed projects are those that are late or behind schedule. On hold projects, on the other hand, are projects that have been temporarily halted.
IMPORTANCE OF BRI

It is only the start. The BRI was launched by China in 2013, but aims to build connectivity and prosperity for all the countries and regions involved. Undoubtedly, China is still a key driver of the BRI, but other countries and their business interests too are getting involved in the programme.

The scale of China’s ambition will engage a bloc of 4.6 billion people, or 61 percent of the world’s population, with a combined GDP of $29 trillion. Trade between China and the BRI nations stood at $6 trillion in 2017, the latest available data shows, and that's likely to expand as new trade connections are created.

“Beneficiary countries are likely to find the most attractive elements of the BRI to be its provision of hard infrastructure. Likewise, the BRI provides China with an opportunity to use its considerable economic means to finance these infrastructure projects around the world,” according to Washington-based Centre for Strategic & International Studies. “The Asian Development Bank (ADB) estimates that the developing countries of Asia collectively will require $26 trillion in infrastructure investment to sustain growth.”

China is rolling out BRI at an important time in the world’s geopolitical transformation. With the United States’ retreating from global affairs and pulling back from aid, loans and infrastructure projects across the world, China is stepping in to fill the void and position itself favourably in the new world order.

But this approach can result in the approval of financially unsound projects, the Saudi research centre noted, while citing the fiscal challenges faced countries such as Pakistan and Laos, where energy loans make up a significant percentage of the government’s foreign debt. It also pointed out that fiscal challenges of BRI participants could also put at risk the sustainability of China’s overseas energy investment.

However, many emerging economies are also keen to tap into China’s growing technological prowess.

Chinese companies also enthusiastically seek to invest in high-tech R&D abroad, aiming to benefit from more advanced financial and human capital and a more consistent business and policy environment, according to London-based think tank Chatham House.

According to the Chatham House report published in November last year, “so far, most of the R&D investment has flown to Europe, North America and China’s rich Asian neighbours, but an increasing amount is now going towards emerging and developing economies, especially those involved in BRI projects... The most popular sectors are semiconductors, AI, aerospace, pharmaceutical and biotech, telecommunications and data science.”

However, China is facing resistance to its ambition to reshape the regional and global order with some countries, both BRI recipients and other donors alike, questioning the structure of BRI projects.

“China’s Belt and Road Initiative (BRI) faces growing skepticism due to concerns regarding corruption, opaque lending practices, and security threats,” a U.S.-China Economic and Security Review Commission stated in a report to the U.S. Congress in November. However, this criticism has not been followed by an outright rejection of BRI because significant infrastructure gaps persist globally and China has few competitors in infrastructure financing.”

Q4 HIGHLIGHTS

In December 2019, the country with the most newly added projects (by value) in the Refinitiv BRI Database was the United Kingdom (UK) with $110.14 billion worth of projects. China is keen to participate in the UK’s massive $82.2 billion High Speed 2 rail project, as it aligns with its ambition to connect Europe with East Asia.

China’s National Development and Reform Commission (NDRC) said that it was under discussions with the UK government for a “wholesale package to build the UK’s second high-speed railway line”.

The state-owned China Railway is also among the bidders for the project, as Beijing attempts to push the BRI further into Europe.

The UK high-speed rail project has two phases. The first covers the route between London and the West Midlands, while the second phases runs from the West Midlands to Leeds and Manchester.
The UK government is also making efforts to woo some of China’s biggest investors to be part of the project as well as a raft of other major UK infrastructure projects. A few years ago, the UK government announced new ‘HS2 partnering day’ between British and Chinese firms to explore joining up on bids for contracts. China’s love for trains is well-documented, given its strong track record in developing fast trains.

In November, China Railway Express crossed into Europe for the first time via Turkey. The new rail link will directly connect Czech Republic’s Prague to Xian, the capital city of Shaanxi Province in central China, via Turkey. The train crossed into Europe using Istanbul’s Marmaray subsea tunnel, reaching the Kazlıçeşme railway station in Zeytinburnu, Istanbul.

The express line crosses two continents, 10 countries, two seas and 11,483 kilometres of road in 12 days with 42 container-loaded wagons.

At the other end of the world, China is also part of a $40 billion liquefied natural gas project on Canada’s West Coast. The project being developed by Royal Dutch Shell Plc. counts PetroChina Company as a 15 percent stakeholder. The project, currently under construction, will connect shale gas from reserves in the province of British Columbia to Chinese and other Asian economies.

“As PetroChina strives to build a diversified oil and gas portfolio, the LNG Canada project is an attractive investment opportunity. The project’s competitiveness, low carbon emissions and relatively short shipping distance to China mean LNG Canada can help supply the increasing demand for gas in China,” Wei Gao, CFO of the China National Oil and Gas Exploration and Development
BRI’S TOP DESTINATIONS

Russia remains the biggest destination for BRI projects, both in terms of number and value of those projects, with 122 projects valued at $287 billion.

“Russia has lobbied for BRI trade corridors to transit its territory and hopes that this will help develop a high-tech industry,” according to the Center for Security Studies (CSS) in Zurich. “From the Russian perspective, as spelled out in a memorandum of understanding between the two countries in 2016, strengthening production and infrastructure in the underdeveloped and thinly settled Far East would be especially desirable.”

The two BRIC nations – a term used to describe the growth markets of Brazil, Russia, India and China by Goldman Sachs at the start of the century – are forging strong economic and security ties to achieve their common goal of influence and economic stimulus in Central Asia and the Middle East.

In September, Russia’s private gas producer Novatek PJSC said it was proceeding with the $21.3 billion Arctic liquefied natural gas (LNG) 2 project, with part of the project’s output earmarked to supply surging Chinese demand. China National Petroleum Corp. holds a 10 percent stake in the ‘Ice Silk Road’ project, with China National Offshore Oil Corp. holding another 10 percent share.

Egypt was second in terms of number of projects with 109 projects valued at just under $100 billion, Refinitiv BRI Database showed. Egypt was ranked 7th in terms of value of projects.

“Chinese companies have been pioneering the development of Egypt’s Suez Canal Economic Zone (SCZone), while further contracts with giant Chinese companies of heavy industries are expected to be announced soon,” newly-appointed Chairman of the SCZone Yehia Zaki told Xinhua in a recent interview.

Work is also under way on the China-Egypt TEDA Suez Economic and Trade Cooperation Zone, a six-square kilometre project that’s expected to attract about 150-180 Chinese enterprises for total investments of $2 billion.

China State Construction Engineering Corporation is also helping build Egypt’s new administrative capital, 50 kilometres each of the capital city of Cairo. The company had started work on 20 skyscrapers in the city’s central business district in mid-2018.

“Some of the skyscrapers have already risen above the ground, including the Iconic Tower, which is currently standing at 80 meters high but is expected to finally exceed 385 meters to become the tallest tower in Egypt and Africa,” Xinhua reported.

In Pakistan, home to the massive China-Pakistan Economic Corridor (CPEC), China is pushing through a number of projects for an investment-starved economy of 200-plus million people.

According to Refinitiv BRI Database, Pakistan has 106 BRI projects under way or planned with a combined value of $117 billion.

In December, Kanwal Shauzab, Pakistan’s Parliamentary Secretary for Planning Development and Reform, told lawmakers that 13 projects valued at around $11 billion dollars had been completed, 13 projects worth $18 billion are under way, and another $21 billion dollar projects were in the pipeline. About 46 percent work on Gwadar East Bay expressway has completed, she said, adding that New Gwadar International Airport is being built with the Chinese grant.

Among Gulf states, Saudi Arabia has emerged as the second biggest destination (in terms of project value) with 106 projects worth $195.7 billion.

China’s BRI initiatives dovetails with Saudi Arabia’s Vision 2030 programme that aims to build new cities, connect the large country via rail and road, and open up underdeveloped promising region such as the $500 billion NEOM City near the Red Sea.

The UAE is another major destination of BRI projects, with $77.86 billion worth of developments under way.

MAJOR SECTORS

Not surprisingly, transportation accounts for 47 percent of all BRI developments, with 1,235 projects valued at $1.8 trillion proposed, planned and under way. The power and water sector is also edging closer to the trillion-dollar mark, with projects worth $893 under way, across 740 developments.

Some of the new power projects announced include 950 megwatt (MW) Dubai Noor Energy 1 Solar Power Plant at the Mohammed Bin Rashid Al Maktoum Solar Park Project in the UAE, two 660 MW Burkit Asam Coal Fired Pithead Power Plant Project in Indonesia and the 3,260 MW Hinkley Point C Nuclear Power Station Project in the UK, according to Refinitiv BRI Database.

Oil and gas projects were also popular as China addressed the twin needs of capital in infrastructure-depleted areas of the Arctic and northern Canada and its own surging demand for natural gas. A few multi-billion-dollar oil and gas projects include the LNG Canada, Yamal Liquefied Natural Gas Project, and Arctic LNG 2 Project.
### Project Sector

<table>
<thead>
<tr>
<th>Project Sector</th>
<th>Project Value (US$/bil)</th>
<th>% of Total Value</th>
<th># of Projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transportation</td>
<td>$1,818.49</td>
<td>46.99%</td>
<td>1,235</td>
</tr>
<tr>
<td>Power &amp; Water</td>
<td>$893.49</td>
<td>23.09%</td>
<td>740</td>
</tr>
<tr>
<td>Real Estate</td>
<td>$436.74</td>
<td>11.28%</td>
<td>596</td>
</tr>
<tr>
<td>Oil &amp; Gas</td>
<td>$418.93</td>
<td>10.82%</td>
<td>140</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>$243.85</td>
<td>6.30%</td>
<td>193</td>
</tr>
<tr>
<td>Mining</td>
<td>$57.98</td>
<td>1.50%</td>
<td>41</td>
</tr>
<tr>
<td>Communication</td>
<td>$0.88</td>
<td>0.02%</td>
<td>20</td>
</tr>
<tr>
<td><strong>Grand Total</strong></td>
<td><strong>$3,870.36</strong></td>
<td><strong>100.00%</strong></td>
<td><strong>2,965</strong></td>
</tr>
</tbody>
</table>

*Source: Refinitiv BRI Database – Up to 31 December 2019*

### Oil & Gas Projects

<table>
<thead>
<tr>
<th>Oil &amp; Gas Projects</th>
<th>Project Value (US$ bil)</th>
<th># of Projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exploration and Production</td>
<td>159.32</td>
<td>31</td>
</tr>
<tr>
<td>Refinery</td>
<td>132.00</td>
<td>45</td>
</tr>
<tr>
<td>Transportation</td>
<td>104.57</td>
<td>43</td>
</tr>
<tr>
<td>Others</td>
<td>10.96</td>
<td>4</td>
</tr>
<tr>
<td>Storage</td>
<td>7.55</td>
<td>11</td>
</tr>
<tr>
<td>Field Support – Offsite and Utilities</td>
<td>4.55</td>
<td>6</td>
</tr>
<tr>
<td><strong>Grand Total</strong></td>
<td><strong>418.93</strong></td>
<td><strong>140</strong></td>
</tr>
</tbody>
</table>

*Source: Refinitiv BRI Database – Up to 31 December 2019*

While physical infrastructure remains central to Beijing’s philosophy of connecting markets, China’s proposed Belt and Road Space Information Corridor, also includes many BRI countries.

“Although China’s Belt and Road Space Information Corridor and Digital Silk Road initiatives may be somewhat vaguely defined, they consist of a number of substantial undertakings in areas from increasing the reliance of BRI countries on Chinese space systems to constructing fiber-optic cable networks connecting key regions,” according to Michael Chase, a senior political scientist at the Rand Corporation and an adjunct professor at the Johns Hopkins University’s Paul H. Nitze School of Advanced International Studies.

“They also could have important implications for the economic and security interests of the United States and its allies and partners. These space and cyberspace initiatives could increase economic dependence on China in ways that give it even greater leverage over participating countries. Just under 50 percent of the projects are master projects valued at $1.8 trillion, as Chinese companies look to supply raw materials, build and finance projects under a single package.
FINANCING OPTIONS

A key criticism of China’s BRI is that it is being financed by Chinese state-owned enterprises, which crowd out local and non-Chinese financial institutions, and gives China unfair advantage and leverage over the projects.

The Chinese government is aiming to address the criticism, and that was evident in the data from Refinitiv BRI Database. Private sector funding accounted for 20.5 percent of all funding data showed, valued at $791 billion. Publicly-listed companies also accounted for $262.5 billion of all funding. However, government institutions led the funding with $1.78 trillion or 46 percent of the total funding allocation.

<table>
<thead>
<tr>
<th>Ownership Type</th>
<th>Project Value (US$ bil)</th>
<th>% of Total Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government</td>
<td>$1,784.87</td>
<td>46.12</td>
</tr>
<tr>
<td>Others</td>
<td>$1,016.92</td>
<td>26.27</td>
</tr>
<tr>
<td>Private</td>
<td>$791.31</td>
<td>20.45</td>
</tr>
<tr>
<td>Publicly Listed</td>
<td>$262.45</td>
<td>6.78</td>
</tr>
<tr>
<td>Foreign</td>
<td>$14.83</td>
<td>0.38</td>
</tr>
<tr>
<td><strong>Grand Total</strong></td>
<td><strong>$3,870.36</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source: Refinitiv BRI Database – Up to 31 December 2019

A number of new projects are being financed by multiple parties and other construction companies as China look to spread the bounty of these projects.

Project financing remains a popular way to fund the projects, with 676 projects structured that way. Loans, primarily from the Chinese government entities, accounted for 192 deals, while mergers and acquisitions (M&A) was also a popular way for Chinese companies to take control of project development.

<table>
<thead>
<tr>
<th>Deal Type</th>
<th>Deal Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Project Finance</td>
<td>676</td>
</tr>
<tr>
<td>Loan</td>
<td>192</td>
</tr>
<tr>
<td>M&amp;A</td>
<td>101</td>
</tr>
<tr>
<td>Bond</td>
<td>31</td>
</tr>
<tr>
<td>Equity</td>
<td>15</td>
</tr>
<tr>
<td><strong>Grand Total</strong></td>
<td><strong>1,015</strong></td>
</tr>
</tbody>
</table>

At the same time, a new report by the Institute of International Finance (IIF) argues that a lot of BRI debt is exposed to countries that are either non-rated by ratings agency, or not of an investment grade.

BRI lending has been accompanied by a hefty external debt buildup in Mongolia, Laos, Djibouti, Cambodia, and the Maldives. While Kyrgyzstan and Timor-Leste have seen robust BRI lending inflows (over 30 percent of their aggregate GDP), the rise in their external debt-to-GDP ratio since 2013 is below the sample average of 8 percentage points, the IIF notes.

“Abundant liquidity spurred by direct loans from China appears to be coinciding with a sharp rise in general government debt in Djibouti, Tajikistan, Mongolia Uzbekistan, the Maldives, Kenya and Pakistan.”

In addition, nearly 45 percent of BRI lending is exposed to significant climate change risks.

“We estimate that some $200 billion of BRI projects to date has been directed to climate-stressed regions, including Maldives, Myanmar, Timor-Leste, Bangladesh, and Ethiopia,” IIF said. “Failing to address physical environmental risks is a significant downside risk for BRI infrastructure projects, highlighting the importance of promoting climate-resilient infrastructure investment.”

Over the past year or so, China has addressed a number of criticisms of BRI such as using its influence over capital-starved vulnerabilities to push through unsustainable projects, leaving many countries in debt. It is also focused on creating projects that add value to local communities and business opportunities for domestic businesses in the BRI countries. But there is a long way to go.

“Domestic constraints on financing and investment, together with criticisms on debt sustainability from both outside and within China, will push China to seek cooperation with foreign companies, international organisations and foreign capital and substantial support from multilateral financial institutions to sustain BRI projects in the coming years,” according to a report by the Centre for International Governance Innovation. “This has the potential to create win-win cooperation on the BRI between China and other developed economies.”
The Belt and Road Initiative (BRI) is one of the largest infrastructure programmes to date in the world covering one-third of the world trade and Gross Domestic Product (GDP) and over 60 percent of the global population. However, like any large programme, it has its own set of economic, social and environmental risks given the amount of money and the scale of projects involved.

The multibillion-dollar scheme, which includes Silk Road Economic Belt (SREB) and the 21st Century Maritime Silk Road (MSR), has received huge traction, with over 125 countries already signing up to implement projects across Asia, Europe, Africa and beyond.

As estimated by the World Bank, when fully implemented, the BRI transport infrastructure can reduce travel times by up to 12 percent and increase trade by between 2.8 and 9.7 percent for corridor economies. It is also expected to lift 7.6 million people from extreme poverty and 32 million people from the moderate poverty.

The World Bank estimates BRI investments across 70 corridor economies (excluding China) to be around $575 billion, including the projects that are already executed, in implementation and under planning.

However, issues relating to project viability and debt sustainability have been major talking points in recent times. Weaker economies, it is felt, may find themselves unable to service their debt obligations if the high-value infrastructure projects fail to achieve the projected economic and social benefits within stipulated time frames. Transparency and access to data are other areas of concern that observers believe need greater attention.
A limited sample survey by Washington-based Centre for Strategic and International Studies had found that more than 60 percent of Chinese-financed BRI projects go to Chinese companies, as stated in the World Bank’s report titled, Belt and Road Economics: Opportunities and Risks of Transport Corridors.

In April 2019, China reaffirmed its commitment at the 2nd Belt and Road Forum to address many of these issues through greater transparency and wider participation.

RISKS AND PITFALLS

There are four key risks: debt sustainability risks; governance risks (corruption and procurement); environmental risks; and social risks, as identified by the World Bank, which conducted an independent analysis of the risks and opportunities of Belt and Road transport corridors.

Accounting firm KPMG agrees that BRI projects are commonly large in scale, complex and bring together multiple stakeholders. “These features present risks across many dimensions,” said Andrew Weir, Senior Partner KPMG in Hong Kong and Global Head of Real Estate & Construction.

The common risks that BRI projects face include procurement, planning, design, construction, operations, financing, handover, economic, environmental, social, political and regulatory.

Given the number of countries involved in the BRI, global law firm Norton Rose Fulbright pointed out that one of the main challenges would be to deal with vastly different legal systems involving the common law, civil law and Islamic law.

“The risks arising from differences in legal systems cut across multi-disciplinary activities and are common regardless of the industries involved,” said Alfred Wu, Partner at firm’s Hong Kong office.
Construction, financial and security are particularly prone because “they usually involve large sums and have long project cycles,” he noted.

As BRI countries vary in terms of economic development, traditions and legal systems, legal experts say these differences give rise to a long list of hurdles for companies looking to invest in overseas infrastructure projects.

“They range from different entry requirements and corporate registration models to capital and labour requirements and land use rights,” said Ai Ai Wong, Chair, Asia Pacific Region at Baker McKenzie.

Often there is a lack of familiarity with the structure and operation of the contractual terms among collaborating countries, as well as limited experience in dealing with contractual settings, “which could heighten the legal risks associated with project management and execution”, she said.

There are political and corruption risks, along with others such as trade sanctions, data privacy and cybersecurity that are typically found in cross-border investments. But Wong says these should not be “deal breakers” and the key is to invest upfront and put in place proper risk identification, management and mitigation measures.

The first phase of the BRI (2013-2018) focussed on large scale infrastructure and construction projects in the energy and transportation sector.

Mukhtar Hussain, Head of Belt and Road Initiative and Business Corridors, Asia Pacific at HSBC, said the primary categories of risks associated with these transactions encompass all the traditional categories of project finance risks, such as completion, currency, construction, financial feasibility and reputational.

“But there were also new elements which came to the fore such as debt sustainability, and the use of local and international partners in the construction of large-scale projects,” he said.

**MITIGATING RISKS**

Given the breadth of risks of BRI projects, KPMG points out that early and comprehensive risk management planning is an important ingredient for success.

The accounting firm takes a four-step approach to project risk management: Identify, Allocate, Mitigate and Quantify.

“First, we identify the full range of risks at an early stage of project planning through research, analysis and project workshops,” said Michael Camerlengo, Partner and Head of Infrastructure for KPMG in Hong Kong.

This is a critical step and involves bringing together the knowledge of experienced local and international experts across each risk area.

As a second step, he said they identify which project stakeholder/s is best placed to manage each risk; whether it be a government body, contractor, insurance agency or otherwise.

“We then develop risk mitigation plans for each, with the goal of reducing the overall risk profile of the project and enhancing overall financial feasibility,” explained Camerlengo.

KPMG’s final step involves quantifying the level of risk using probability and statistical analysis, as well as expert insights.

“Having the right people, with the right knowledge at the planning stage is critical to ensure this approach is effective and maximises the chances of ensuring all risks are captured and fully addressed,” Camerlengo added.

Legal experts agree that understanding the regime one is dealing with and understanding the investor’s regime is crucial to identifying and addressing this risk.

“In terms of the investee regime, enforcement against sovereign assets is key,” said Wu of Norton Rose Fulbright.

Given that many developing states operate on the basis of the absolute immunity theory, he pointed out that enforcement against the investee state within that state is often problematic.

Therefore, Wu suggested, an investor may need to look for assets of the investee state situated offshore for enforcement purposes. “These should preferably be assets situated in more stable and well-developed jurisdictions which practise the restrictive theory of sovereign immunity.”
DISPUTE RESOLUTION

Another important risk reduction measure that experts suggest is to adopt a body of governing law and a dispute resolution mechanism which will lead to transparent and predictable processes of dispute resolution and enforcement. Norton Rose Fulbright suggests the use of arbitration seated in a New York Convention jurisdiction should be considered.

In terms of the investor, Wu said one should understand the anti-bribery and sanction rules in its home jurisdiction which govern overseas investments.

Given that many of these home rules will not only regulate home activities but will have extra-territorial effects, he said a thorough understanding of the practice and enforcement policies of the regulators and the interpretation of the law by the court is important.

Since different legal systems and traditions are present across the BRI countries, experts noted that Chinese companies are now recognising the value of having strong local partner support throughout the project development.

However, Wong of Baker McKenzie pointed out that the issue of cultural misalignment between the parties is often overlooked. “It is not uncommon for Chinese businesses to take a different approach to project development from their counterparts.”

Therefore, Wong suggested, getting the approach right and making an agreement with the key project stakeholders, such as governments, utilities and local regulators, is critical to the success of the project.

Experts feel building strong, trusting relationships with all key stakeholders will help ensure the expectation of doing business “the right way” is well communicated and minimise companies’ risk exposure.

“Also, it’s important to engage advisers who know what the risks look like on the ground as this will allow companies to be fully prepared should any unexpected challenges arise,” said Wong.

While the circumstances of each jurisdiction are different and depend on a range of local factors, HSBC’s Hussain said there are examples of international best practice which can be adopted to ensure consistency of process and outcome.

As an example, he said, the use of international tendering will encourage competitive bidding and the promulgation of internationally accepted standards for sustainability such as green financing.

Large projects like BRI also pose environmental and social risks, with World Bank estimating that transport infrastructure increases carbon dioxide emission by 0.3 percent worldwide – but by 7 percent or more in some countries as production expands in sectors with higher emission.

Although ESG (Environmental, Social, and Governance) as a concept is rapidly gaining momentum in the global business community, KPMG’s Weir said that when it comes to planning and delivering major projects around the world, there is still room for improvement and the BRI is no exception.

He said he expects these dimensions to become fully embedded aspects of planning for BRI projects in the not-too-distant future.
Need for greater flexibility in the project structure

When it comes to commercial structures for a BRI project, industry experts feel there is “no one size fits all”. The approach should be specific for each project based on the risks, returns and policy objectives behind the project.

“In general, structures that include greater flexibility and partnership characteristics are more likely to reach favourable outcomes in the event of project underperformance,” said KPMG’s Camerlengo.

For example, he says, an approach being increasingly implemented in developed markets – which may have useful application for BRI projects – is target construction cost contracts. These involve both the contractor and project owner sharing an element of the upside and downside of the end construction outturn cost. “This approach can be effective in encouraging transparency and teamwork,” he said.

Some experts are of the view that joint ventures (JVs) can be useful structures when the primary objectives of local project owners/governments and foreign participants are mostly financial in nature. However, they warn this model can encounter difficulties if the broader objectives of the parties are not aligned.

“For example, the local project owner is primarily focused on social policy outcomes, but the foreign partner/partners are focused on financial outcomes. At an overall level, ensuring transparency and alignment of objectives at the project outset is a critical success factor for any project,” said Dennis Zhang, Partner and Head of Valuations for KPMG in Northern China.

In terms of JV structure, experts say this could be either an incorporated JV or an unincorporated JV – both have advantages and disadvantages.

Norton Rose Fulbright’s Wu also noted that proper mechanisms for the operation of the JV management board, veto powers for important matters, JV accounting, the mechanisms for the funding of and withdrawal of funds from the JV, and the process for terminating and unwinding the JV will need to be carefully considered and built-in.

As a recent trend, it’s been observed that Chinese developers are increasingly looking beyond Chinese lenders for more competitive sources of funding.

“They are becoming less willing to provide parent company guarantees that Chinese lenders have traditionally sought in order to mitigate lending risks. Instead, Chinese developers now see the benefit of limited or non-recourse project financing and the competition that using international lenders brings to the lending terms,” said Wong.

Chinese companies also recognise the advantages of involving international companies and lenders who bring vast experience in and knowledge of doing projects in many BRI countries.

As part of the drafting of a contract, Wong said companies need to ensure they have the proper risk management and risk allocation provisions supported by clearly set out liability language.

“Any unclear language in the dispute resolution clause, for example, can render the whole provision uncertain and unenforceable,” she warned.
DEBT SUSTAINABILITY OF BRI PROJECTS

China has signalled that it is committed to international standards for ensuring debt sustainability of Belt and Road projects.

The Belt and Road Initiative (BRI) promises to transform the world’s economic landscape, but apprehensions have been expressed whether weaker economies can derive real benefits as the multibillion-dollar projects face debt sustainability issues.

A World Bank analysis that looked at all BRI debt revealed that 12 of 43 low- and middle-income countries (for which detailed data are available) would experience a deterioration in their medium-term outlook for debt sustainability. In addition to issues relating to debt sustainability, countries executing BRI projects worth $1 billion or more tend to face other risks typically associated with megaprojects.

According to World Bank estimates, 36 out of the 45 corridor economies/countries with identified investments have investments exceeding $1 billion, with about half the total invested in energy and mining and a fourth in transport and shipping.

“These projects are highly likely to experience large cost overruns and severe delays, which could become large future liabilities for the governments of corridor economies,” stated The World Bank in its report titled, Belt and Road Economics: Opportunities and Risks of Transport Corridors, released last year.

Mukhtar Hussain, Head of Belt and Road Initiative and Business Corridors, Asia Pacific at HSBC, said the issue of debt sustainability is a fundamentally important consideration for each country to make when assessing project-related opportunities.

While domestic ministries may well have developed basic financial models and projections, he suggested that this can then be reviewed by specialist industry consultants and international bodies (such as World Bank, Asian Development Bank, and International Finance Corporation) to obtain robust external inputs and sensitivities.
“Governments can also choose to hire banks who have specialist project finance/public finance capabilities to advise on funding structures through the capital markets,” said Hussain.

He said these avenues provide channels for countries to robustly evaluate financing feasibility and fiscal prudence before committing to transactions.

ADAPTABLE SUSTAINABILITY

Michael Camerlengo, Partner and Head of Infrastructure for KPMG in Hong Kong pointed out that foreign enterprises that enter a market and provide debt funding for a project often end up being scapegoats if that project fails – particularly those projects that result in debt for equity swaps.

However, he said, every debt transaction always involves two parties – a borrower and a lender – “so the onus is on both groups to ensure the funding structure adopted is sustainable and suitable from the outset.”

In the case of BRI projects, Camerlengo said that participating governments need to be mindful of their existing and projected levels of public debt – exercising caution where existing public debt levels are high, or the project in question is of such scale that it would have a significant negative impact on the public balance sheet if it were to fail.

Project financial feasibility and economic impact analyses can be highly valuable for participating governments to make this assessment, added Dennis Zhang – Partner and Head of Valuations for KPMG in Northern China.

In terms of the latter, he said understanding the broader benefits that a project will generate for the economy – including tax receipts, trade benefits, and economic growth – can help to assess whether the additional public debt is worth the extra risk.

Global law firm Norton Rose Fulbright Hong Kong suggests that the approach to debt sustainability should be “proper due diligence” and the ability to be “adaptable and think out of the box.”

“Understanding a regime’s credit history and creditworthiness requires due diligence,”

said Alfred Wu, Partner at Norton Rose Fulbright Hong Kong.

He adds that the willingness to take cash alternatives, such as concession rights, production of natural resources, etc. in place of cash for repayment of debts requires adaptability and thinking out of the box.

The Chinese authorities have made important announcements in recent times to reaffirm that future BRI transactions will be “open, green and clean.” For instance, China published a BRI Debt Sustainability Framework (BRI DSF), partially based on World Bank–IMF Debt Sustainability Framework for low-income countries, at the 2nd Belt and Road Forum in April 2019. The step was aimed at enhancing the analysis of debt sustainability, fiscal risks, and debt reporting transparency for BRI projects.

Hussain said adopting and adhering to international best standards is a benchmark which China is committed to, but he insists that international organisations will have an important role to play in harnessing their respective expertise and inputs into this area.
INCLUSIVE INVOLVEMENT IN BRI 2.0

Greater collaboration and inclusivity are expected to be the hallmarks of the next phase of the Belt and Road Initiative (BRI).

Faced with questions from various quarters about the sustainability of the Belt and Road Initiative (BRI) projects, China’s President Xi Jinping promised at the 2nd BRI Forum in April 2019 to address transparency concerns and open BRI to wider participation.

While it remains to be seen what actual steps China will take based on the messages delivered at the 2nd BRI Forum, Alfred Wu, Partner at Norton Rose Fulbright Hong Kong, said it is unlikely that those are just “empty talks” for cosmetic purposes.

He said China is concerned about its international image and the need to recalibrate the BRI to tone down “the China presence” in other countries and to address calls from the international community for “open, green and clean” approaches to procurement policies.

“Steps taken by China will undoubtedly be nuanced,” he said.

As announced by the President, China wants this next era of BRI – BRI 2.0 – to be open, clean, and green. “BRI 2.0 is about being transparent, sustainable, high quality, beneficial to local economies, and open to international participation,” said Mukhtar Hussain, Head of Belt and Road Initiative and Business Corridors, Asia Pacific at HSBC.

“We have seen a real focus and intensity to ensure international projects are open and inclusive in terms of international involvement, and that the financing behind these projects is robust enough to attract capital from multiple sources,” he said.

Most observers feel China will take all possible steps to iron out any structural flaws BRI might have as it’s only in their interest to ensure these projects become successful.
“There are growing signs suggesting that China is taking a more collaborative approach to BRI projects, both at the policy level and also by Chinese enterprises,” said Ai Ai Wong, Chair, Asia Pacific at Baker McKenzie.

She gave the example of an MoU signed between the Ministry of Finance of the People’s Republic of China and several Multilateral Development Banks (MDBs) in March 2019 to create the Multilateral Cooperation Centre for Development Finance (MCDF), which is intended to promote investments in connectivity and infrastructure in underdeveloped regions within the framework of the BRI.

“Chinese enterprises are also increasingly willing to partner with other local and international players who bring with them the market knowledge and experience of doing projects in many BRI countries,” said Wong.

As a positive development, KPMG said they noticed a sizeable uptick in inquiries from both Chinese State-Owned Enterprises (SOEs) and multi-national companies. “In the case of the latter, several major client groups have approached us to help develop strategies to access BRI projects and develop SOE partnerships,” said Michael Camerlengo, Partner and Head of Infrastructure for KPMG in Hong Kong.

FINANCING GAP

Interestingly, this has included groups in financial services, utilities, and professional services – all of whom are global industry leaders in their industry, he said.

The approaches taken by Chinese SOEs are also evolving. Dennis Zhang, Partner and Head of Valuations for KPMG in Northern China, pointed out that Chinese SOEs are enhancing their collaboration with global infrastructure and energy corporations, financial institutions and professional firms, and generally adopting a more open mindset towards international cooperation.

“We also see greater volumes of Chinese SOEs with an appetite for renewable energy and sustainable development projects, placing a greater emphasis on commercial feasibility at an early stage and raising funds through more diverse sources such as international commercial banks, multilateral development banks and other private sources of capital,” he said.

Another reason why China would seek the participation of private financing is that there is a significant infrastructure financing gap in emerging markets in Asia. According to Asian Development Bank (ADB) estimates, the region needs an injection of $1.7 trillion per year from 2016 to 2030.

“Despite China’s deep financial resources, there’s a clear need to mobilise more private infrastructure financing from the likes of banks, private equity, and the capital markets,” said Hussain.

He believes that increasing emphasis on international standards and being commercially viable will help make it possible to encourage broader participation and attracting international organisations and multilateral lenders.

“But the recipient countries also need to demonstrate political stability, strong rule-of-law, and effective anti-corruption regulations,” he said.
SUSTAINABLE FINANCE IN INFRASTRUCTURE PROJECTS

China’s focus on promoting green financing could open opportunities for sustainable financing innovations in Belt and Road projects.

At the 2nd Belt and Road Forum for International Cooperation, held in Beijing in April 2019, Chinese President Xi Jinping said that BRI must be green and sustainable, and environmental protection must underpin the initiative “to protect the common home we live in.”

The summit saw 27 global financial institutions sign up to the Green Investment Principles for the Belt and Road (GIP). Jointly launched by the China Society for Finance and Banking, and the City of London’s Green Finance Initiative in November 2018, these voluntary principles call upon lenders, investors and corporates that invest and operate in the Belt and Road regions to ensure their projects are aligned with the requirements of environmental sustainability and the Paris Agreement.

On September 11-12, 2019, at the fourth edition of the Belt and Road Summit in Hong Kong, a high-level panel, comprising of public and private entities, discussed the business case for adopting sustainable finance in infrastructure projects, BRI included, and the latest trends in this regard.
KEY TAKEAWAYS FROM THE PANEL DISCUSSION WERE AS FOLLOWS:

- Infrastructure, as an asset class, requires substantial investment over a long-term horizon.
- Infrastructure assets are integrated within the environment; they employ large workforces, many of whom are exposed to dangerous work, and they operate under regulatory frameworks that require good governance.
- The Environmental, Social and Governance (ESG) risks associated with the lifespan of an infrastructure project, from design to construction, financing, and operation, directly impact the financial and operational performances of businesses and assets.
- ESG is critical in the context of BRI because infrastructure development is at the heart of belt and road projects. Responsible investment can not only help avoid ESG risks but also generate positive values such as achieving resource efficiencies, reducing environmental footprint, creating jobs, improving community relations, and getting long-term risk-adjusted returns.
- Infrastructure fund managers have traditionally focused on the risk side of social responsibility to prevent environmental and social incidents. The standard investment decision-making process included consideration of the company’s health and safety track record and environmental due diligence at the point of investment, and after that, regular audits on an ongoing basis to ensure compliance with regulations, and minimisation of ecological footprint.
- Climate risk is being incorporated into investment decision-making not only from an ecological point of view but also from a financial sustainability standpoint. For example, traditional forms of conventional energy are increasingly under scrutiny in the face of falling costs of renewable energy, which has resulted in infrastructure investment funds instituting policies that limit their exposure to coal-fired power.
- Incorporating ESG into investment decision-making also creates opportunities to take a long-term view on the future development of clean energy, and of emerging areas like renewable hydrogen, where cheap renewable power is used to produce hydrogen, one of the potential fuels for future.
- Meanwhile, investors are looking at opportunities for implementing sustainable initiatives across their asset portfolio in areas like materials recycling, energy efficiency, and vehicle fleet optimisation. For example, Macquarie Infrastructure and Real Assets (MIRA) reviewed energy use in the airports in its portfolio and initiated projects to transition from traditional to LED lighting for energy savings.
- Management teams are being made accountable for ESGs through Key Performance Indicators (KPI) tied to executive remuneration; increasingly, a significant part of those KPIs include non-financial metrics.
- One of the challenges of measuring ESG impact has been the lack of data. The fund management industry has tried to address the data deficit by moving towards voluntary disclosure through initiatives such as Global Real Estate Sustainability Benchmark (GRESB), which assesses and benchmarks the ESG performance of real assets, providing standardised and validated data, which is then disclosed to investors.
- The investor community is increasingly a big demand driver of issuance into the ESG market. They are demanding that frequent issuers offer ESG products, and that is driving up volumes.
- China’s plans to transform itself into one of the leading forces of green finance and energy are expected to influence BRI projects and help the efforts of participating countries to transition to low carbon economies.
- A welcome development has been the increased role of sovereign issuers in sustainable finance. The Chinese government pioneered this trend in 2014-2015. Before that, the global green bond market was mostly market-led.
- China Green Finance Committee, which comes under the China Society for Finance & Banking, has developed the green bond catalogue, which lists the type of projects eligible for sustainable financing.
- The Asia-Pacific green bond market has been dominated by China. Green bond issuance in the international bond market grew from $14 billion in 2013 before the Green Bond Principles (GBP) were announced to $180 billion in 2018. the International Capital Market Association (ICMA) is expecting about $250 billion in issuance in 2019, with the Asia Pacific accounting for about 20 to 30 percent of this issuance, driven mainly by China.
- When compared to the $100 trillion of issuance in the international bond market, the $680 billion in issuance so far over the entire lifetime of the green bond market is relatively small, which is indicative of the growth possibilities in this market.

In conclusion, adopting sustainable investment practices for BRI infrastructure projects not only helps to address ESG risks but also generates positive value for investors, employees, and the citizens and societies that will use the infrastructure. Sustainable finance strategies not only reduce risks but enhance value and the entire society.
Chinese firms should be well-prepared to tackle the challenges and risks associated with big construction and real estate projects in the Gulf region under the Belt and Road Initiative (BRI).

New investment opportunities are emerging for Chinese firms in the Gulf Cooperation Council (GCC) as member countries explore alternative means to finance construction and real estate (CRE) projects.

“There is a growing market for public-private partnerships (PPP) in the region as the CRE sector looks at alternative ways to finance the completion of these projects,” said Gan Mei, Director, and China Desk Lead at PwC Middle East.

Most GCC countries are enacting PPP laws and embarking on initial projects, which could be an attractive opportunity for Chinese State-Owned Entities (SOEs) with access to export credit guarantee schemes and financing, she said.

China’s President Xi Jinping proposed a package of $20 billion in loans, and about $106 million in financial aid, to Middle East countries, at the 2018 China-Arab States Cooperation Forum, as Beijing wants to revive the region’s economy through various schemes including BRI.

To capitalise on the regional opportunities, Mei said, Chinese companies need to understand local development strategies and government initiatives, such as the Saudi Vision 2030 or the Kuwait National Development Plan 2035 (KNDP).

“They also need to understand more specialised local policies and targets, including smart city strategies and building technology initiatives where China can showcase the innovation from some of their fast-growing cities such as Shenzhen,” she said.

China has been making huge capital expenditure over the past several years, with 13.4 percent of its Gross Domestic Product (GDP) in 2015 going towards developing economic and social infrastructure, compared to an average 3.2 percent in other BRICS countries, according to International Monetary Fund (IMF) estimates.
“This has provided key learnings for the Chinese, building a leadership position in innovation and application of emerging technologies within the infrastructure and construction space,” said Ravi Suri, KPMG Global Head of Infrastructure Finance and Regional Head of Infrastructure Advisory, MESA.

He cited the example of Chinese companies that are at the forefront in the application of 3D printing, bioplastics, and prefabricated prefinished volumetric construction. Some newer urban developments in China also exhibit high standards of sustainable design and architecture, concepts that resonate regionally and globally.

“These concepts have massive potential in the GCC construction market where an increasing number of construction and real estate development is undertaken at a significant scale with sustainability being a key theme,” said Suri.

SPECIALISATION IS THE KEY

Mei agreed that specialisation and sophistication would be a key factor for developers, particularly in markets like Dubai, where the development market is maturing but slowing down with decreasing property prices, the recent halt on Al Maktoum Airport construction and government calls for fewer new developments. These are clear signals that a focus on quality over quantity will increasingly become a competitive advantage for developers.

“Any strategy for the Middle East region must be up to date and agile, customised to selected local markets as there is no cookie-cutter approach for the region. It has to be updated constantly and even with variations from city to city,” she said.

Suri suggests major Chinese developers and contractors form a partnership with local firms to create a differentiated value proposition in the market as the GCC has many prominent regional developers and construction companies with international experience.
MITIGATING RISKS

Industry experts acknowledge that there are challenges pertaining to some of the larger CRE projects for the local and Chinese companies involved. However, these depend on the nature of projects and geographies.

“Focusing on local needs and local engagement as well as understanding Chinese policy and interest will help mitigate risks and timely execution of projects,” said Suri, adding that financing and compliance standards should also be aligned with international best practices.

He said BRI is an evolving programme and includes a good deal of funding through government-to-government (G2G) debt financing tied to sovereign guarantees, in addition to the participation of the state-owned entities and financial institutions.

“However, we are now seeing an increased propensity of Chinese institutions to partner with multi-lateral, bilateral and commercial financial institutions as well as increasing participation in syndicates,” he said.

Another critical challenge for BRI would be the speed at which these initiatives are going to be implemented, said Dana Salbak, Director Research for MENA at JLL.

“BRI is a five to 15-year investment, which means returns will be delayed, and therefore investors need to look long-term and think beyond a short-term cycle,” she said.

Due to the nature of the construction industry, which is generally high value and long-term return investments, PwC’s Mei points out that working capital and cash flow can be preserved and optimised through the implementation of efficient tax processes which will help debunk the “debt trap” stereotype associated with CRE projects.

MANAGE TAX COMPLIANCE

Mei said the Gulf market remains attractive to Chinese investors due to, amongst other incentives, lower tax rates applicable across the Gulf region and the eligibility to claim the Value Added Tax (VAT) paid on expenses in countries where VAT has been implemented.

With the recent implementation of VAT in the UAE, Saudi Arabia, and Bahrain, Mei said Chinese companies need to efficiently manage their tax affairs and compliance similarly to other international tax jurisdictions.

Suri points out that the GCC’s relative financial strength, combined with a focus on balancing risk allocation between stakeholders and optimising financing structures, has the potential to effectively reduce financial risks, which have affected Chinese and some host countries in the past.

He recommends credit and potential risk insurance mitigation tools for BRI projects, including export credit financing, risk cover, the participation of alternative funds including infrastructure and pension funds, and innovative financing tools such as efficacy insurance where new technology risks are involved.

Mei pointed out that Chinese companies can further safeguard themselves by ensuring good governance and tax management to counter any potential adverse impact on operations with a careful selection and appraisal of investments, which are generally accepted mechanisms for businesses to safeguard key interests.

“Considering the opportunity for CRE projects, Chinese companies would benefit from strategic planning together with obtaining specialised tax advice in advance to streamline and optimise operations in the region,” she said.
INTERVIEW

BRI OPPORTUNITIES GALORE FOR GULF ARAB STATES

Gulf governments are actively positioning their countries as integral to the Belt and Road Initiative (BRI).

China’s mega trillion-dollar Belt and Road Initiative (BRI) proposes six economic corridors, but none includes any official agreement with the Gulf Cooperation Council (GCC).

Guided by the historic Silk Road route and linking Asia, Africa, and Europe, the ambitious new global trade route, will intersect in the Middle East.

The oil-rich Gulf Arab states will play a crucial role in building the hard and soft infrastructure of BRI, given their strategic location, rapid population growth, and expected robust economic growth.

Concurrently, the five major BRI priorities – policy coordination, infrastructure connectivity, unimpeded trade, financial integration, and connecting people – aligns with the vision programs of the various GCC governments, according to the European Bank for Reconstruction and Development (EBRD).

The strategic importance of the region is reflected in Beijing already signing BRI-related construction agreements with six Arab countries, according to an Emirates Diplomatic Academy report. The scheme, along with strategic partnerships with eight Arab states, propelled investments to an estimated $29.5 billion in 2016, making China the largest investor in the Middle East, an October 2018 report posted on the website of The Arab Gulf States Institute in Washington (AGSIW) noted.

That said, the total value of BRI projects, launched in 2013 by Chinese President Xi Jinping, stands at $3.67 trillion (£2.83 trillion), according to data from Refinitiv. So far, 126 countries and 29 international organisations have signed cooperation agreements with China.

By mid-2019, China had signed agreements with 21 MENA countries (including 18 Arab states) on joint BRI projects, according to a European Council on Foreign Relations (ECFR) report issued in October last year.

Refinitiv | BRI Connect: An Initiative in Numbers
In an interview, AGSIW Resident Scholar Robert Mogielnicki said all Gulf governments are seeking to tap into BRI development initiatives and are actively positioning their countries as integral links connecting Asia with European and African markets.

As BRI-related countries strive to boost a global development strategy and focus on creating sustainable infrastructure projects, China’s Digital Silk Road initiatives may offer Gulf Arab states with new opportunities to drastically improve the efficiency of existing infrastructure and boost productivity with a minimal carbon footprint, Mogielnicki noted.

Excerpts from the interview

Q: How much importance are Gulf Arab states giving on building sustainable infrastructure?
Governments across the Gulf Arab region place a high priority on infrastructure development that is sustainable on two levels: economic and environmental. Following the drop in oil prices in 2014-15, regional governments sought to reduce wasteful spending on unnecessary development schemes.

However, Gulf Arab governments continued to spend heavily on infrastructure initiatives to boost growth, generate jobs, and attract foreign direct investment.

The environmental component of sustainable development projects in the Gulf has traditionally taken a back seat to economic feasibility and demand considerations; however, economic concerns are playing an increasingly important role in regional development schemes.

Q: Which Gulf Arab states are focusing on building sustainable infrastructure?
All Gulf Arab governments hope to tap into BRI development initiatives and are actively positioning their countries as integral links connecting Asia with European and African markets. The United Arab Emirates is among the best-suited of Middle Eastern and North African states to integrate sustainable infrastructure development into BRI projects. The UAE possesses a Minister of Climate Change and Environment who helps align economic policy with environmental goals as well as Masdar City in Abu Dhabi, where a rapidly growing clean-tech cluster is taking shape.

Given the scale of its economy and demographic weight, Saudi Arabia has the potential to be a significant regional player in the development of sustainable infrastructure, but projects have been slow to move from the conceptual stages to implementation.

Q: How is Dubai developing sustainable infrastructure?
The emirate of Dubai has aligned its government policy and the commercial activity of its state-owned entities to accomplishing sustainable infrastructure development. The emirate’s 50-Year Charter addresses the issue of self-sufficient homes and aims to ensure that at least one-tenth of citizens’ homes are self-sufficient in terms of water, food, and energy. The Dubai Electricity and Water Authority is responsible for installing solar panels on at least 10 percent of Emirati homes, in addition to carrying out the Dubai Clean Energy Strategy 2050, which aims to produce 75 percent of Dubai’s total power output from clean energy.

China is a natural economic partner to support Dubai with specific initiatives, such as outfitting homes with solar panels, as well as long-term renewable energy and sustainability initiatives. China accounted for 45 percent of the world’s renewable energy investments in 2017, and is, by many accounts, the world’s renewable energy superpower. Dubai government awarded a contract to China’s Shanghai Power and Saudi Arabia’s ACWA Power to build a 700-megawatt extension to the Mohammed bin Rashid Al Maktoum Solar Complex; the project will make the Dubai-based solar complex the largest in the world.

Q: What new opportunities will BRI offer in the coming years?
China’s Digital Silk Road initiatives may present Gulf Arab states with new opportunities to drastically improve the efficiency of existing infrastructure and boost productivity with a minimal carbon footprint. There is substantial demand from Gulf Arab governments for technology platforms and services from China that can reduce waste and streamline public sector services.
RENEWABLE ENERGY MARKERS FOR BELT AND ROAD

BRI projects must be fed by renewable energy instead of fossil fuels like coal and oil, according to Francesco La Camera, Director-General, International Renewable Energy Agency (IRENA).

The Chinese government launched the Belt and Road Initiative (BRI) in 2013 to promote regional development and connectivity. While the initiative has primarily focused on the development of transport infrastructure like railways and ports and power plants, it is also true that these projects require massive amounts of energy.

The region covered by BRI has significant potential to be powered by solar energy, according to a study published in July last year in the journal Joule. The study, supported by Tsinghua University and the Harvard Global Institute, among others, found that less than four percent of the maximum solar potential of the region could meet the BRI’s electricity demand for 2030.

The study, which covered 66 BRI countries connected geographically, found that their 2030 electricity needs could be satisfied by converting only 3.7 percent of the region’s solar energy at an investment of $11.2 trillion.

Research by China’s National Development and Reform Commission (NDRC), which oversees the BRI, found that the projected installed capacity of renewable energy for 38 countries in BRI could reach 644 gigawatts (GW) from 2020-2030, and total investment in wind and solar power could reach $644 billion, based on their targets for renewable energy.

While China has provided financing for renewables projects overseas, including in Belt and Road countries, it is a small share compared to the percentage for other areas such as oil, gas and coal, NDRC’s energy policy manager, international programme Han Chen wrote in a blog post in April 2019.
Citing a joint report by World Resources Institute (WRI) and Boston University, issued in October 2018, Han noted that out of the loans in the energy sector for BRI, 43 percent of state policy bank loans by the China Development Bank and Export-Import Bank of China went to oil, gas and petrochemicals, 18 percent to coal, but only 3.4 percent to solar and 2.9 percent to wind from 2014-2017. Coal power, nuclear power, and hydropower loans combined were almost seven times more than loans to solar and wind.

Moreover, Chinese companies’ direct overseas greenfield investments and acquisitions in the power sector (as opposed to loans) in BRI countries were skewed in favour of coal, oil, and gas-fired power plants.

On the other hand, a 2019 report by The Global Commission on the Geopolitics of Energy Transformation found that in aggregate, China is the world’s largest producer, exporter and installer of solar panels, wind turbines, batteries, and electric vehicles, placing it at the forefront of the global energy transition. The Commission, which is backed by the International Renewable Energy Agency (IRENA), said China also leads the world in renewable energy patents.

IRENA’s Director-General Francesco La Camera told Zawya in January that China accounts for a large part of global investment in renewables.

IRENA’s Future of Solar report had noted that in Asia, the world’s biggest solar market, China accounted for 62 percent of the region’s installed solar capacity of 280 GW in 2018.

“We are working with them to review their long-term planning. I hope we will be successful in adding more renewable energy in their new [five-year] plan,” he said.

He also reminded that China is investing heavily in electric vehicles, which he attributed to the government’s focus on reducing the problem of pollution. The market share of electric vehicles in the country increased from 4.5 percent to 4.7 percent, according to data released by the China Association of Automobile Manufacturers (CAAM) in January.

“In this case, the PPM [parts per million] is also a conducive role in CO2 reduction. I think it is important to make clear that in BRI, no coal plant is to be funded.”

In an earlier interview with Zawya in June 2019, he had pointed out that at the Annual General Meeting of the China Council for International Cooperation on Environment and Development (CCICED) in Hangzhou the same month, IRENA had recommended that the BRI must be fed by renewable energy instead of fossil fuels like coal and oil.

“That was our intervention during the meeting where we called for more involvement of renewables,” he had said.

‘10 Years: Progress to Action’, a data booklet published for the 10th annual Assembly of IRENA, said annual renewable energy investment needs to double from around $330 billion today, to close to $750 billion to deploy renewable energy at the speed required. It said much of the needed investment could be met by redirecting planned fossil fuel investment, adding that close to $10 trillion of non-renewables related energy investments are planned to 2030, risking stranded assets and increasing the likelihood of exceeding the world’s 1.5-degree carbon budget this decade.
PAKISTAN REDUCES POWER DEFICIT WITH BELT AND ROAD INVESTMENTS

The number of coal-fired power plants in Pakistan have increased under the Belt and Road Initiative (BRI) but the government should also aim to tap China’s clean energy expertise.

The $62 billion China-Pakistan Economic Corridor Project (CPEC) is one of the most ambitious undertakings of the sprawling $4 trillion BRI that aims to connect Europe, Asia and Africa through a network of seaports, airports, railways, roads and infrastructure developments such as power generation.

To date, 22 CPEC projects with a combined value of $18.9 billion have either been initiated or completed. Further, 15 power sector projects with a combined value of $20.9 billion are expected to be completed in 2020.

A vast majority of the projects in Pakistan have been in the power sector given the country’s chronic power shortages. Generation and transmission projects make up seven of the 11 CPEC projects completed and six of the 11 CPEC projects under construction at the end of 2018.

Three-quarters of the new generation capacity to be added by the CPEC power sector projects are from coal-fired power plants, which would raise coal’s share in Pakistan’s power generation mix from three percent in 2017, to 20 percent by 2025.

This focus on coal has been criticised by analysts as it belies Beijing’s pledge to develop sustainable BRI projects.

“There are concerns that BRI infrastructure, especially coal power plants, will negatively impact the environment in a variety of ways, including by harming the global climate and polluting air and water,” said a report by Erica Downs, a senior research scholar at the Centre on Global Energy Policy at Columbia School of International and Public Affairs (SIPA).

The push to produce more electricity from coal stands in contrast to the move away from coal for power generation in most countries over the past few years. Pakistan was ranked 11th among countries that are actively building new coal projects, according to a report by Global Energy Monitor.
In fact, the global coal demand is expected to decline to 4,350 metric tonnes per year by 2025, compared to 5,357 metric tonnes if the world pursues sustainable energy projects, according to the International Energy Agency (IEA).

"Investment in new coal-fired power plants in 2017 was at its lowest level in a decade, not least because of a drop of more than 50 per cent in such investment in China, which has pledged to reach a peak in CO2 emissions by 2030 or earlier," the IEA said in its annual World Energy Outlook. "The projection for coal-fired power generation is essentially flat over the period to 2040, putting related investment on a downward trajectory."

SWITCHING TO COAL

Interestingly, Pakistan has no other option but to rush to coal to cut its ballooning energy imports. The South Asian nation of 200 million population had a power deficit of 2,969 MW in 2017, but it has come down from a peak of 6,785 MW in 2012. CPEC aims to raise capacity by another 16,040 MW, wiping off the deficit.

Over the past few decades, Pakistan built its power capacity based on imported oil, which has led to considerable financial distress as oil prices jumped to record levels and remain volatile. The country on average spends $3 billion to $3.5 billion on oil imports, according to a quarterly CEPC report published by the government.

A few renewable energy projects are also under way, including the 100 MW Quaid-e-Azam Solar Park in Bahawulpur, Punjab, a 100 MW wind farm and a 50 MW wind farm which are both operational in Thatta, Sindh, among others.

However, the large-scale projects are coal-based, including the 300 MW power project in the port city of Gwadar, two Engro Thar Block II 330 MW coal-fired power plant in Sindh, two 660M coal-fired power plant in Sahiwal, Punjab, two 660MW coal-fired power plants at Port Qasim in Karachi, 1,320 MW coal-fired power plant in Hub, Balochistan.

BEIJING’S INTEREST

Downs attributes CPEC focus on coal to China’s considerable expertise in developing coal power plants and its excess capacity.

China’s state-owned financial institutions are also supporting the development of overseas coal-fired power plants. "As of July 2018, Chinese banks and firms had committed or provided funding for more than 25 per cent of all coal plants under development outside of China. Pakistan was the fourth largest recipient of Chinese financing for coal-powered plants behind Bangladesh, Vietnam, and South Africa,” he said.

Pakistan, which is keen to tap into its own vast coal reserves in the Thar Desert, is also taking advantage of China’s speedy loan approvals and financing instruments that making the proposition for the Pakistani government – under pressure from its citizens to tackle chronic blackouts – hard to resist.

However, Downs warns that these power and other infrastructure projects could push the country into a debt-trap, adding to its more than $100 billion in foreign debt.

While the CPEC power projects should pay for themselves as consumers start paying their bills, the Chinese and other financial institutions are lending money to special purpose companies (SPCs) established to develop the projects, which makes the Pakistani government liable for the debt.

“Pakistan’s sovereign debt is likely to increase if the government has to honour the sovereign guarantees it issues to back the development of CPEC power projects,” Downs noted. “Some of these sovereign guarantees support the payment obligations of the Central Power Purchasing Agency (CPPA) to the power producers.”

Most of these liabilities are in foreign currencies which could even be more gruelling for a country whose currency has already been decimated by devaluations and trade weakness in recent years.

Despite some concerns about CPEC under the new government in Islamabad led by Prime Minister Imran Khan, the country approved a CPEC authority to fast-track projects and unlock the potential of the interlinked production network and global value chains through regional and global connectivity.

“The completion of CPEC will not only benefit Pakistan and China but also the entire region,” Prime Minister Khan had said in August, adding that the timely completion of CPEC projects was the top priority of the government and CPEC is a clear example of joint efforts and partnership between Pakistan and China.

While the Pakistani government and other stakeholders in the country’s electricity sector would have to decide the energy mix that serves the country best, the BRI provides a great opportunity to diversify the energy mix in favour of clean energy, an area where China is an undisputed global leader.
The UAE’s emergence as a regional hub for Belt and Road has put the country on the destination map of Chinese real estate investors.

Chinese appetite for real estate investments in the UAE is expected to continue to rise in 2020, with Abu Dhabi set to join Dubai in attracting new buyers following the UAE capital opening up the freehold property ownership to foreigners.

The second biggest economy in the Middle East is the eighth most popular country in the world for Chinese buyers as ranked by the number of real estate buying enquiries by the Chinese, according to Juwai IQI that runs China’s leading international property website juwai.com.

“Chinese buyer enquiries hit a peak in the first quarter of 2019. Since then, the demand has declined, although it remains at nearly triple the average level of 2018,” said Juwai IQI Executive Chairman Georg Chmiel.

“In 2018, Chinese buyers acquired an estimated $617.07 million worth of residential real estate in Dubai. We don’t think the boom is over yet, and we expect Chinese buyer inquiries to grow further in 2020,” he said and added that Chinese residential investment in the Gulf and especially in the UAE grew in 2019.

David Ji, Head of Research & Consultancy, Greater China at Knight Frank, pointed out that Chinese investors’ targets are very diverse and careful these days as “the country is curbing rampant trophy asset buying.”

“Middle Eastern countries offer natural resources as well as financial market potential, attracting buyers from China. However, they are still feeling the market out and being open-minded in terms of investment targets,” he said.
Developments in the UAE have attracted Chinese property investors. This was evident during the 20th Luxury Property Show in Shanghai in December 2019, when the Dubai Land Department received around 10,000 enquiries from Chinese investors.

Imran Hussain, Head of Residential Valuation at Colliers International MENA, said there had been significant interest from Chinese investors over the past few years in particular within a few developments, such as Motor City, the Greens, and Jumeirah Lake Towers.

“We are noticing a further growth in confidence for the Dubai property market from Chinese nationals as interest from this segment is more pronounced throughout Dubai rather than in just a few developments,” he said.

VALUABLE SEGMENT

Chinese buyers are seen as a valuable segment of the investment and end-user market. Many brokerage firms and other property-related service providers are employing Chinese nationals to service this segment.

Chinese brokerage firm Fidu Properties, for instance, opened its first regional office in Dubai in 2018, followed by the second office in October last, to cash in on the growing Chinese interest in UAE’s property market.

Nazish Khan, COO of Fidu Properties, said the UAE has several luxurious sightings and investments to offer across a range of individual specifications and budgets.

“Going by the responses over the past couple of months, it can be presumed that this trend will continue in 2020 also,” he said.

ABU DHABI, A NEW FRONTIER

A significant change the market is expecting this year is the emergence of Abu Dhabi, the UAE’s capital, as a destination for Chinese buyers, given that freehold ownership is now possible, said Chmiel.

“Abu Dhabi has great potential as an exciting market for Chinese buyers. Growth in demand could be very rapid,” he said, adding that developers will need to bring the right kind of products onto the market, and some regulatory issues still need to be sorted out.

“We are watching anxiously to see what moves the industry and regulators in Abu Dhabi make to attract Chinese buyers. It’s potentially a very appealing market for our investors,” he said.

KEY DRIVERS

Industry experts say that UAE’s strengthening socio-political and trade relations with China has played a part in boosting Chinese investment into the emirate’s real estate sector.

“The UAE being the key component of BRI and strategic ties between the two nations have given renewed confidence to two-way investments,” said Alan James Gammon, general manager at Samana Group, which expects to attract $1 billion worth of investments from China in the next five years.

The Dubai-based developer announced last October that it would be launching three new real estate projects till the first quarter of 2020, with the first China office set to come by March-April 2020.

“These developments [BRI and bilateral trade] and Expo 2020 have given us enough reasons to go aggressive and promote our property and investment services in the Chinese market,” he said.

Industry players say the rise of preferential UAE policies for the Chinese has been playing an indirect role in boosting and attracting Chinese investors and buyers.

This has helped even young companies like Fidu Properties to grow fast over the past year.

“We aim to grow at a constant rate of 10 percent every year in order to reach our goal and become number one on all levels. The response so far has been overwhelming,” said Khan, adding that greater than 50 percent proportion rate comes from the Chinese investors.

For greater sustainability and transparency, Dubai’s Real Estate Regulatory Agency (RERA) in November 2019 issued a law that stipulates the developers will no longer collect service charges from investors for the upkeep of the properties. “It gives yet another benefit to investors, along with higher yields,” he said.
MARKET STRATEGY

To capitalise on the growing Chinese interest in the UAE, local brokerages like fam Properties are focusing on a Business-to-Business (B2B) strategy. “The response has been good so far,” said Firas Al Msaddi, CEO, fam Properties, and fam Living.

He said it is a very competitive market as the Chinese have access to other real estate markets in Japan, Vietnam, and Thailand.

The company is aiming to generate 25 percent of its revenue from the Chinese market over the next three years.

UAE companies are adopting various means, including hosting roadshows in the main Chinese cities to promote Dubai and their products.

Samana, which recently held roadshows in Shanghai, Beijing, and Guangzhou cities, said it witnessed a high level of interest from the Chinese in opening a business in the UAE.

“Chinese buyers are a key market for us across our range of businesses. We anticipate bi-monthly visits to China to promote products and services,” said Gammon.

The company envisages 70 percent of sales for its latest project, Samana Golf Avenue will come from the Chinese market.

Other Dubai-based developers are also seeing a spike in demand from Chinese buyers. For instance, Sobha Realty last year opened a sales office in Shanghai as it recorded 200 percent growth in Chinese investors for its Sobha Hartland project in the first two months of 2019, with over 36 percent of buyers for the project from China.

Dubai-based Ellington Properties, too, is looking at China seriously and has already signed a partnership with Beike, China’s leading open platform real estate listings portal, which will take its properties to potential investors in over 300 cities in the country.

Binghatti Developers is looking to tap into the Chinese market, with the opening of a new office in Hong Kong.

PROPERTY TYPES

Fidu Properties says Chinese investors are interested in mainly ready and off-plan properties. “While considering such properties, they tend to centrally narrow down the factors to location, annual yield, and selling prices,” said Khan.

Downtown Dubai, Greens, and the International City fulfill these requirements and a predominance of Chinese investors and communities can be witnessed here.

While Fidu Properties doesn’t customise its offerings as its central aim is to promote the listings and attract buyers, Khan said they do hand out special prices and packages for the Chinese investors and buyers.

Gammon says Chinese investors prefer ready properties, and the Samana Greens project fits the bill. “Chinese are also very interested in the residency programmes in Dubai and the UAE, which they can secure through property investment.”

According to fam Properties, Chinese are generally interested in income/rental generating units, with a price range averaging 1 million to 1.5 million UAE dirhams ($272,242 to $408,363) per unit.

In terms of offering attractive deals, Al Msaddi said they are working with one property developer to create a guaranteed income scheme for Chinese investors. “We also offer a lot of educational and logistic support to our Chinese investors,” he added.

Chmiel said apart from retail investors, Chinese institutional buyers too can be tapped. However, “they tend to work through partnerships with local developers,” he explained. “They have resources available to them that the average retail buyer does not. Chinese buyers tend to like water views, convenient access to transportation and amenities, and luxury finishes and services.”
PRODUCTION TEAM

Zawya editorial
Sayed Husein
Syed Amen Kader
Bhaskar Raj
Anoop Menon
Anita Iyer

Refinitiv data teams
Bill Feng

Report consultants
Walid El-Tigi
Mike Rautmann

Refinitv content teams
Lauren Reilly
Saira Kanwar
BRI Connect, a part of Refinitiv’s Global Infrastructure Initiative, is a suite of evolving tools that provides access to comprehensive information including macroeconomic, market, financing, geopolitical, country and operational risk data on BRI related countries, organisations, deals and projects.

Available exclusively through Eikon, BRI Connect helps financial professionals to:

• monitor a database of BRI related projects, updated in real-time
• access unparalleled coverage of financing deals and primary capital markets
• better understand where to invest in BRI opportunities
• secure accurate, up-to-date country risk ratings
• details on over 3500 BRI related organizations

BRI METHODOLOGY

Our methodology for identifying projects related to BRI is as follows:

BRI Connect includes projects that have been identified as such by the Chinese government or Chinese State Departments, or where project contractors have signed agreements with the government departments of the relevant country along BRI Corridors and have obtained relevant regulators’ approvals required for Belt & Road initiatives, or which are published on the BRI official website: yidaiyilu.gov.cn/ or projects that have direct Chinese participation at a consultant, owner, contractor and financer level or are of strategic interest located along a BRI Economic Corridor.